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PASS TREASURY AND FRB

E.O. 11652: N/A

TAGS: EFIN, IT

SUBJECT: ASSESSMENT OF NEW ITALIAN ECONOMIC PROGRAM

REF: A. ROME 1678, B. ROME 1450, C. ROME 1945, D. ROME 2014,
E. ROME A-37

SUMMARY. FOLLOWING REPORT ASSESSES MONETARY POLICIES
ALREADY ADOPTED BY ITALIAN AUTHORITIES AND CONOMIC
POLICY PROPOSALS CONTAINED IN CHRISTIAN DEMOCRATS'
(DC) ECONOMIC PROGRAM. (REPORT MAY BE USEFUL IN
CONNECTION WITH REVIEW OF ITALIAN SITUATION IN OECD'S
WP-3 ON FEBRUARY 16-17 AND WITH CURRENT IMF CONSIDERATION
OF NEW STANDBY FOR ITALY.) EVENTUAL FATE OF DC
ECONOMIC PROGRAM IS VERY UNCLEAR AT THIS STAGE,
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GOVERNMENT (GOI) AND BANK OF ITALY (BOI) ARE STILL
CALCULATING STATISTICAL IMPLICATIONS OF VARIOUS

ECONOMIC MEASURES AND PROPOSALS. CONSEQUENTLY, EMBASSY HAS HAD TO MAKE SOME OF ITS OWN VERY ROUGH ESTIMATES, WHICH SHOULD BE USED WITH CAUTION. ON BALANCE, GOI MONETARY MEASURES SHOULD BE GIVEN FAIRLY HIGH SCORE. FISCAL PROPOSALS ARE ABOUT MINIMUM ACCEPTABLE. FOREIGN EXCHANGE POLITICS, ESPECIALLY CLEAN FLOAT, SHOULD BE QUITE HELPFUL EVENTUALLY IN DEALING WITH ITALY'S BALANCE OF PAYMENTS PROBLEM. INFLATION PROBLEM, INCLUDING ADVERSE EFFECT ON IMPORT PRICES OF DEPRECIATING LIRA, IS STILL VERY WORRISOME. INITIAL EFFORTS TOWARD ADOPTION OF INCOMES POLICY ARE QUITE FEEBLE, BUT ARE BETTER THAN NOTHING AND COULD AT LEAST OPEN THE DOOR TO LONG-DELAYED SERIOUS EFFORT TO DEAL WITH THIS PROBLEM. END SUMMARY.

1. MONETARY POLICY.

A. INTEREST RATES. GOI HAS ALREADY EMPLOYED ALL THREE CLASSIC MONETARY INSTRUMENTS--DISCOUNT RATE, OPEN MARKET OPERATIONS AND RESERVE REQUIREMENT. DISCOUNT RATE WAS RAISED FROM 6 TO 7 PERCENT (REF A), WITH MAXIMUM PENALTY RATES REMAINING AT 3 PERCENT ABOVE DISCOUNT RATE. SHORT-TERM INTEREST RATES (E.G., INTER-BANK RATES) HAD ALREADY BEGUN TO RISE BEFORE MONETARY MEASURES WERE TAKEN, REFLECTING DEMAND FOR CREDIT TO FINANCE CAPITAL FLIGHT AND RUSH TO OBTAIN CREDIT BEFORE MONETARY AUTHORITIES TOOK NEW RESTRICTIVE ACTION. FOLLOWING RISE IN DISCOUNT RATE, SHORT-TERM MARKET RATES HAVE CONTINUED TO RISE RATHER SHARPLY. OPEN MARKET OPERATIONS TOOK FORM OF BANK OF ITALY BIDDING AGAINST COMMERCIAL BANKS UNDER NEW TREASURY BILL AUCTION SYSTEM SO AS TO FORCE UP RATES (REF B). ALTHOUGH PRIME RATE SET BY BANK CARTEL HAS NOT BEEN CHANGED FROM CURRENT 12 PERCENT LEVEL, MONETARY AUTHORITIES WILL REPORTEDLY TALK TO LARGER BANKS THIS WEEK TO CONSIDER QUESTION. DE FACTO PRIME RATE HAD PREVIOUSLY BEEN IN 10 TO 11 PERCENT RANGE BECAUSE OF AMPLE LIQUIDITY. RATE HAS APPARENTLY ALREADY RISEN SOMEWHAT, WITH PRESS SUGGESTING NEW CARTEL RATE OF AT LEAST 13 PERCENT. DIFFERENTIAL UNCOVERED INTEREST RATE IN FAVOR OF MILAN (VERSUS LONDON 90-DAY DOLLAR RATE) HAS RISEN CONSIDERABLY. (CALCULATION OF COVERED RATE IS NOW DIFFICULT DUE TO UNRELIABILITY OF FORWARD EXCHANGE RATE DATA.)
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PURPOSE OF INTEREST RATE INCREASES, ESPECIALLY SHORT-TERM RATES, IS TO EXERCISE MODERATE RESTRAINT ON EXPANSION OF DOMESTIC LIQUIDITY AND TO INCREASE DIS-INCENTIVE TO EXPORT CAPITAL WITHOUT NIPPING ECONOMIC RECOVERY IN THE BUD. RELATIVE MODERATION IN USE OF MONETARY POLICY REFLECTS LATTER CONSTRAINT BUT IS ALSO PARTLY DUE TO POLITICAL PRESSURES AGAINST NEW "CREDIT CRUNCH."
FOLLOWING TABLE SHOWS GENERAL RISE IN SHORT-TERM INTEREST RATE LEVELS.

1/20/76 2/9/76

DISCOUNTS AND ADVANCES	6.00	7.00
3 MONTHS TREASURY BILLS		
(SECONDARY)	7.851	9.801
3 MONTHS INTER-BANK RATE	8.000	9.875
UNCOVERED DIFFERENTIAL VS		
DOLLAR IN LONDON ON ANNUAL		
BASIS	2.375	4.250

B. RESERVE REQUIREMENT. BANK RESERVE REQUIREMENT ON DEMAND DEPOSITS HAS BEEN INCREASED FROM 15 TO 15.75 PERCENT (REF C). FORCED PORTFOLIO INVESTMENT REQUIREMENT (30 PERCENT OF INCREASE IN DEPOSITS) HAS NOT BEEN CHANGED. (REQUIREMENT IS ACTUALLY 28-29 PERCENT WHEN CALCULATED ON NOMINAL VALUE OF SECURITIES AND, LIKE RESERVE REQUIREMENT, HAS EFFECT OF TYING UP FUNDS OTHERWISE AVAILABLE FOR BANK LENDING.) ESTIMATED EFFECT OF INCREASE IN RESERVE RATIO DURING 1976 IS TO ABSORB 750 BILLION LIRE, WITH CORRESPONDING REDUCTION IN BANK CREDIT EXPANSION. HOWEVER, HEAD OF BOI RESEARCH OFFICE FAZIO THOUGHT THAT DOMESTIC CREDIT EXPANSION CEILING OF 31,000 BILLION LIRE AGREED TO WITH EC (UNDER EC MEDIUM-TERM CREDIT CONDITIONS) NEED NOT BE REVISED UNTIL PERIODIC REVIEW TAKES PLACE AND THAT SAME CEILING MIGHT BE EMBODIED IN IMF STANDBY AGREEMENT. FAZIO JUSTIFIED RETENTION OF OLD CEILING ON GROUNDS THAT RESERVE REQUIREMENT CHANGE WAS MERELY MEANT TO ABSORB TEMPORARY BULGE IN LIQUIDITY AND MIGHT BE REVERSED. ON OTHER HAND, ALL OTHER THINGS BEING EQUAL, IF BANK CREDIT EXPANSION WERE REDUCED BY 750 BILLION LIRE, THIS WOULD HAVE EFFECT OF REDUCING PERCENT INCREASE IN DOMESTIC CREDIT EXPANSION FROM 18.8 PERCENT (OVER 1975'S ESTIMATED 26,100 BILLION LIRE) TO 15.9 PERCENT.

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2. FISCAL POLICY.

A. TAXES. MAIN ASPECTS OF FISCAL POLICY PART OF DC ECONOMIC PROGRAM (REF D) CONSIST OF 75 PERCENT EXCESS PROFITS TAX, 2,000 BILLION LIRE STANDBY TAX PACKAGE AND FORCED INVESTMENT IN TREASURY BILLS OF INCREASED INCOME EARNED BY CERTAIN UPPER INCOME EMPLOYEES. (RISE IN INCOME OF LATTER EMPLOYEES WOULD BE LIMITED TO INCREASES DUE TO AUTOMATIC COST OF LIVING ADJUSTMENTS AND SENIORITY INCREASES ONLY.) EXCESS PROFITS TAX AHS BEEN PORTRAYED AS DISINCENTIVE TO EXCESSIVE PRICE INCREASES BY BUSINESS AND AS ALTERNATIVE TO ADMINISTRATIVELY UNWORKABLE PRICE FREEZE. REVENUE IS EVENTUALLY TO BE USED TO FINANCE PROPOSED INDUSTRIAL RESTRUCTURING PLAN. NO ESTIMATE OF AMOUNT OF REVENUE WHICH WOULD BE GENERATED IS AVAILABLE. WHILE THIS "PRICE CONTROL" MEASURE MIGHT BE DEFENDED ON GROUNDS THAT IT WAS POLITICALLY NECESSARY IN ORDER TO TAKE ANY "WAGE CONTROL" MEASURES, IT IS HARDLY DESIRABLE IN ITSELF, SINCE IT COULD

VERY WELL DISCOURAGE INVESTMENT IMMEDIATELY NEEDED FOR
ECONOMIC RECOVERY BY THOSE FIRMS WHICH ARE MOST
EFFICIENT, IN ORDER TO FINANCE LESS EFFICIENT-- FIRMS.

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STANDBY TAX PACKAGE WOULD ONLY BE EMPLOYED AT SOME
UNDETERMINED FUTURE TIME WHEN ECONOMIC RECOVERY IS
SUFFICIENTLY UNDERWAY TO MAKE IT CLEARLY DESIRABLE TO
REDUCE EXPANSIONARY EFFECTS OF LARGE CASH BUDGET DEFICIT.
PRECISE CONTENT TO PACKAGE DOES NOT SEEM TO HAVE BEEN
THOUGHT OUT IN DETAIL AND POSSIBLE INCREASE IN VALUE ADDED
TAX (IVA) ON NON-ESSENTIALS, ESPECIALLY IMPORTS, HAS
ALREADY BEEN TRIED IN 1974 TAX PACKAGE WITH UNCERTAIN
RESULTS. PROSPECTS FOR PARLIAMENTARY APPROVAL OF TAX PACKAGE
ARE DOUBTFUL. ALSO, IT DOES NOT SEEM LIKELY THAT ENOUGH
NEW REVENUE WOULD BE COLLECTED DURING 1976 TO PERCEPTIBLY

REDUCE LARGE CASH BUDGET DEFICIT (ESTIMATED AT 14,800 BILLION LIRE FOR PURPOSES OF EC LOAN AGREEMENT).

B. TREASURY BILL FINANCING. BASED ON BOI STUDY OF LIMITED OFFICIAL USE
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DISTRIBUTION OF INCOME IN 1974, EMBASSY HAS MADE ROUGH CALCULATION OF NEW FINANCING AVAILABLE TO COVER BUDGET DEFICIT THROUGH FORCED INVESTMENT OF SALARY INCREASE IN TREASURY BILLS. NO DECISION HAS YET BEEN MADE ON CUT-OFF LEVEL OF SALARY INCOME ABOVE WHICH RISE IN INCOME WOULD BE LIMITED TO AUTOMATIC EFFECTS OF COST OF LIVING AND SENIORITY INCREASES. HOWEVER, IF SALARY LIMITATIONS WERE IMPOSED ON INCOMES OF 5 MILLION LIRE OR MORE IN 1975 (AS HAS BEEN RUMORED) AND IF TOTAL COST OF LIVING AND SENIORITY INCREASES AMOUNTED TO ABOUT 16 PERCENT IN 1976, THEN INCREASE IN THIS SALARY BILL WOULD BE ABOUT 2,615 BILLION LIRE. THIS SUM WOULD, THEREFORE, BE AVAILABLE FOR INVESTMENT IN TREASURY BILLS. UNDER GOI COMMITMENTS TO EC, AMOUNT OF 1976 TREASURY DEFICIT OF 14,800 BILLION LIRE WHICH COULD BE FINANCED BY CENTRAL BANK COULD AT LEAST THEORETICALLY BE REDUCED FROM 5,700 BILLION LIRE TO 3,085 BILLION LIRE.

3. FOREIGN EXCHANGE POLICY. MOST IMPORTANT ELEMENT OF FOREIGN EXCHANGE POLICY WAS GOI DECISION TO SUSPEND CENTRAL BANK EXCHANGE MARKET INTERVENTION ON JANUARY 21 SO AS TO PERMIT CLEAN FLOAT. OTHER TWO EXCHANGE CONTROL MEASURES: (A) REDUCING PERIOD DURING WHICH FOREIGN EXCHANGE HELD IN FOREIGN CURRENCY ACCOUNTS MUST BE SOLD TO ITALIAN EXCHANGE OFFICE AND (B) CREATING FOREIGN CURRENCY ACCOUNTS FOR ITALIAN EMIGRANTS ARE RELATIVELY UNIMPORTANT. (FIRST MEASURE COULD HAVE CONSIDERABLE SHORT-LIVED EFFECT ON EXCHANGE MARKET DUE TO FEBRUARY 11 DEADLINE FOR SALES OF BALANCES OF PERHAPS \$150-\$200 MILLION IN ALL EXISTING ACCOUNTS.) APPROVAL IN DECEMBER 1975 OF SLIGHT LIBERALIZATION OF PAYMENTS TERMS ON IMPORTS AND EXPORTS (REF E), NO DOUBT, HAD SOME ADVERSE EFFECT ON LIRA DURING SPECULATIVE PERIOD PRIOR TO WITHDRAWAL OF BOI FROM MARKET, GIVEN LARGE SIZE OF ITALY'S IMPORTS AND EXPORTS. MEASURE HAS BEEN SOURCE OF CONSIDERABLE CRITICISM AND CONTROVERSY (E.G., AS TO WHETHER TREASURY MINISTRY WAS ADEQUATELY CONSULTED BY MINISTRY OF FOREIGN TRADE BEFORE MEASURE WAS TAKEN). FAILURE OF GOI TO REVERSE THAT DECISION SEEMS BASED ON NEED TO SAVE FACE OF MINISTER OF FOREIGN TRADE, ASSUMPTION THAT DAMAGE HAS ALREADY LARGELY BEEN DONE AND BELIEF THAT PAYMENT PERIODS IN EFFECT PREVIOUSLY WERE REALLY TO RESTRICTIVE IN TERMS OF ALLOWING LIMITED OFFICIAL USE
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ITALIAN EXPORTERS TO GIVE SUFFICIENTLY ATTRACTIVE CREDIT TERMS AND PERMITTING IMPORTERS TO BEGIN TO RE-STOCK DEPLETED INVENTORIES IN ANTICIPATION OF RECOVERY. THERE HAS ALSO BEEN PRESSURE ON GOI TO "DO SOMETHING" ABOUT SPECULATROS, E.G., THROUGH CLOSER SCRUTINY BY BANKS OF TRADE AND PAYMENTS DOCUMENTS TO AVOID OVER AND UNDER-INVOICING AND THROUGH TIGHTER CONTROLS AT BORDERS. BANKS, WITH SOME JUSTIFICATION, CLAIM THAT THEY ARE NOT TECHNICALLY COMPETENT NOR DO THEY HAVE PERSONNEL SUFFICIENT TO EXERCISE TIGHT CONTROL OF IMPORT AND EXPORT PRICING. ALSO, VERY LARGE VOLUME OF BORDER TRAFFIC BOTH OF TOURISTS AND OF EMIGRANT WORKERS MAKES CONTROL IN THAT AREA VERY DIFFICULT. FINALLY, IT SHOULD NOT BE FORGOTTEN THAT ITALY ALREADY HAS BODY OF RATHER COMPREHENSIVE AND RESTRICTIVE EXCHANGE CONTROL REGULATIONS ON BOOKS, E.G., 500,000 LIRE PER YEAR TOURIST ALLOWANCE FOR ITALIAN RESIDENTS AND 50 PERCENT NON-INTEREST BEARING DEPOSIT ON MOST CAPITAL OUTFLOWS. IN FINAL ANALYSIS, DEPRECIATED EXCHANGE RATE SHOULD BE MOST EFFECTIVE MEASURE IN THIS FIELD, ESPECIALLY FOR ITALIAN EXPORTS OF MIDDLE-LINE MANUFACTURED GOODS, FOR TOURISM AND POSSIBLY FOR SOME DIRECT INVESTMENT CAPITAL INFLOWS. ON OTHER HAND, THERE IS WIDE BELIEF THAT ITALIAN IMPORTS ARE NOT VERY PRICE ELASTIC BECAUSE THEY CONSIST IN LARGE PART OF FOOD, FUELS, INDUSTRIAL RAW MATERIALS AND SOPHISTICATED CAPITAL GOODS. IN ANY CASE, EXPECTED "J CURVE" EFFECT OF LIRA DEPRECIATION WILL MEAN THAT INITIAL IMPACT ON BALANCE OF PAYMENTS OF DECLINING LIRA WILL BE ADVERSE. EMBASSY IS FAIRLY OPTIMISTIC, HOWEVER, ABOUT ULTIMATE FAVORABLE EFFECT. FOLLOWING TABLE SHOWS (A) WEIGHTED AVERAGE DEPRECIATION OF LIRA (BOI MEASUREMENT) BEFORE AND AFTER BEGINNING OF CLEAN FLOAT AND (B) ROUGH MEASURE OF CHANGE SINCE BEGINNING OF CLEAN FLOAT IN PRICE COMPETITIVENESS OF ITALIAN EXPORTS IN ITALY'S MAIN EXPORT MARKETS IN LOCAL CURRENCY. LATTER PERCENTAGE CHANGE COVERS PERIOD SINCE SMITHSONIAN EXCHANGE RATE RE-ALIGNMENT IN DECEMBER 1971 (BASED ON RELATIVE CHANGES IN WHOLESALE PRICES ADJUSTED BY EXCHANGE RATE MOVEMENTS).

TABLE 2 - LIRA EXCHANGE RATE; EXPORT PRICE COMPETITION
(PERCENT CHANGE)
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A. LIRA DEPRECIATION SINCE 2/73:

ALL CURRENCIES	21.01	27.59
DOLLAR	15.40	22.33
EC	25.27	31.90

B. CHANGE IN PRICE COMPETITIVENESS
IN:

GERMANY	-11.6	2.9
FRANCE	-9.9	2.6
UNITED KINGDOM	-14.9	-6.8
UNITED STATES	-13.2	-2.7

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4. INCOMES POLICY. DC ECONOMIC PROGRAM CALLS FOR COMPLETE FREEZE ON "MANAGERS" SALARIES AND LIMITATIONS ON UPPER INCOME EMPLOYEES' SALARIES TO COST OF LIVING AND SENIORITY INCREASES OVER TWELVE MONTH PERIOD. (IN LATTER CASE SALARY INCREASES WOULD HAVE TO BE INVESTED IN TREASURY BILLS DURING THIS PRIOD. SEE ABOVE.) BASED ON COMMENTS BY PROF. ANDREATTA (ECONOMIC ADVISER TO PRIME MINISTER WHO HELPED DRAFT DC PROGRAM), PRESS SPECULATES THAT SALARY CUT-OFF WILL ENVENTUALLY BE SET AT ANNUAL INCOME OF 5 MILLION

LIRE OR MORE. EMBASSY ELABORATION OF BOI STUDY OF INCOME DISTRIBUTION IN 1974 SUGGESTS THAT THIS GROUP OF INCOME EARNERS WOULD ACCOUNT FOR ABOUT 10 PERCENT OF ALL WAGE AND SALARY INCOME IN 1975. WITHIN THIS GROUP, ABOUT 0.5 PERCENT OF INCOME EARNERS REPRESENTING ABOUT 4 PERCENT OF LIMITED OFFICIAL USE

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TOTAL WAGE AND SALARY INCOME WOULD BE IN INCOME BRACKET OF 12.5 MILLION LIRE OR MORE AND MIGHT BE CONSIDERED TO BE "MANAGERS" AND THEREFORE SUBJECT TO COMPLETE SALARY FREEZE. TABLE 3 SHOWS EMBASSY ASSUMPTIONS ABOUT WAGE RATE INCREASES BEFORE AND AFTER INCOMES POLICY PROPOSALS. THESE RATES ARE THEN WEIGHTED BY APPROXIMATE DISTRIBUTION OF INCOME AMONG THESE SALARY LEVELS. RESULTING INCREASE IN TOTAL WAGE BILL IN 1976 WOULD THUS HAVE RISEN BY ABOUT 18 PERCENT BEFORE PROPOSED GOI MEASURES, COMPARED TO 13 PERCENT AFTER THESE MEASURES. THIS FIGURE COMPARES WITH: 14.5 PERCENT IN 1971, 11.2 PERCENT IN 1972, 20.4 PERCENT IN 1973, 24.1 PERCENT IN 1974 AND PRESUMED 20 PERCENT IN 1975. EMBASSY HAS VERY SERIOUS DOUBTS ABOUT EVENTUAL APPROVAL OF THIS PART OF PROGRAM BY PARLIAMENT AND ABOUT COOPERATION OF LABOR UNIONS IN MAKING IT WORK. HOWEVER, IF THESE ASSUMPTIONS SHOULD BE ANYWHERE NEAR THE MARK, EFFECT IN MODERATING RISE IN LABOR COSTS WOULD BE GREATER THAN EMBASSY HAD INITIALLY EXPECTED. (REF D).

TABLE 3 - 1976 INCREASES IN WAGE AND SALARIES (PERCENT CHANGE)

	BEFORE	AFTER
INDEPENDENT LABOR	15	5
DEPENDENT LABOR:	20	17
OF WHICH:		
OVER 12.5 MILLION LIRE	15	-
5-12.5 MILLION LIRE	20	16
9-5 MILLION LIRE	20	18
NET NATIONAL INCOME	18	13

5. COMMENT. FUTURE OF DC PROPOSALS IS STILL VERY MUCH IN DOUBT, AS OPPOSITION TO INDIVIDUAL PARTS OF PROGRAM MAY BE ENCOUNTERED WHEN SPECIFIC PROPOSALS ARE PRESENTED TO UNIONS, POLITICAL PARTIES AND PARLIAMENT. CONSIDERABLE TIME WILL BE REQUIRED UNDER BEST OF CIRCUMSTANCES IN PREPARING AND GETTING MEASURES APPROVED. MONETARY MEASURES ARE PROBABLY AS GOOD AS CAN BE EXPECTED, GIVEN NEED TO AVOID UNDERCUTTING ECONOMIC RECOVERY AND POLITICAL SENSITIVITY TO "CREDIT CRUNCH." HISTORICALLY, RESTRICTIVE MONETARY MEASURES HAVE BEEN QUITE EFFECTIVE IN REDUCING EXCESS DEMAND AND IMPROVING BALANCE OF PAYMENTS. HOWEVER, LIMITED OFFICIAL USE

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CONSTANTLY INCREASING SIZE OF TREASURY BUDGET FINANCING PROBLEM HAS GRADUALLY REDUCED LEEWAY AVAILABLE TO BOI IN CONTROLLING LIQUIDITY. FISCAL MEASURES, IF NOT ACTUALLY PERNICIOUS (E.G., EXCESS PROFITS TAX), MAY WELL BE LONG WAY OFF IN TERMS OF PARLIAMENTARY APPROVAL, WILL BE HARD TO ENFORCE AND WILL HAVE UNCERTAIN REVENUE EFFECTS. STILL, AT LEAST SOME ATTEMPT HAS BEEN MADE TO ATTACK GROWING CASH BUDGET PROBLEM, EVEN AT TIME WHEN IT CAN BE ARGUED THAT EXPANSIONARY FISCAL POLICY IS JUSTIFIABLE FOR CYCLICAL REASONS.

6. SOME DEPRECIATION OF LIRA WAS PROBABLY INEVITABLE IN 1976 REFLECTING BOTH ASSUMED WORSENING OF BALANCE OF PAYMENTS DUE TO ECONOMIC RECOVERY AND PERSISTENTLY GREATER LABOR COST INCREASES IN ITALY THAN AVERAGE INCREASE FOR OTHER INDUSTRIAL COUNTRIES. CURRENT DEPRECIATION AGAINST DOLLAR OF ABOUT 10 PERCENT MAY BE SUFFICIENT IN SHORT RUN. HOWEVER, UNLESS SOME CONTROL OF LABOR COSTS CAN BE IMPOSED, ITALY MAY WELL BE FORCED TO ADOPT A DE FACTO "CRAWLING PEG." INFLATIONARY IMPLICATIONS OF SUCH A POLICY ARE WORRISOME. (DEVALUATION OF 10 PERCENT IS ESTIMATED TO RESULT IN 3-4/5 PERCENT PRICE INCREASE). IN ANY CASE, EARLIER AND PERHAPS LARGER DEPRECIATION OF LIRA THAN MIGHT OTHERWISE HAVE OCCURRED SHOULD, AFTER INITIAL ADVERSE EFFECT ON COST OF IMPORTS, BE QUITE POSITIVE. EXCHANGE CONTROL MEASURES MAY BE marginally HELPFUL, BUT ARE A WEAK REED TO LEAN UPON IN ITALY.

7. FINALLY, EFFORTS BY GOI TO ADOPT SOME KIND OF INCOMES POLICY IS LONG OVERDUE, GIVEN EXTREMELY HIGH WAGE RATE INCREASES WHICH HAVE OCCURRED SINCE "HOT AUTUMN" OF 1969. SHARP RISES HAVE OCCURRED BOTH IN NOMINAL AND IN REAL TERMS. EVEN AS RECENTLY AS 1973, WHEN PRICE CONTROLS WERE EMPLOYED, NO SERIOUS EFFORT WAS MADE TO ARREST RAPID RISE IN WAGE AND SOCIAL INSURANCE COSTS. IT IS TYPICAL THAT LABOR UNION AND SOCIALIST INFLUENCE HAVE FORCED INCLUSION OF COMPLETE SALARY FREEZE ON MANAGERIAL CLASS AS TRADE-OFF FOR POSSIBLE ACCEPTANCE OF SOME LIMITS ON LOWER LEVEL INCOMES. UNION SPOKESMEN ARE NOW FIERCELY DEFENDING PRINCIPLE OF FREEDOM OF COLLECTIVE BARGAINING AND ONE LEADER HAS SUGGESTED THAT SALARY LIMIT SHOULD ONLY APPLY ABOVE 12.5 MILLION LIRE LEVEL. STILL, THERE DOES SEEM

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TO BE SOME WILLINGNESS BY UNIONS TO MODERATE WAGE DEMANDS. GOI SHOULD BE ENCOURAGED BY USG AND IMF IN CONSULTATIVE MEETINGS AND IN NEGOTIATION OF ANY FINANCIAL ASSISTANCE TO MAKE

STRONG EFFORT TO IMPLEMENT MEASURES IN BUDGET AND INCOMES
FIELDS.VOLPE

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TAGS: EFIN, IT
To: STATE
Type: TE
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